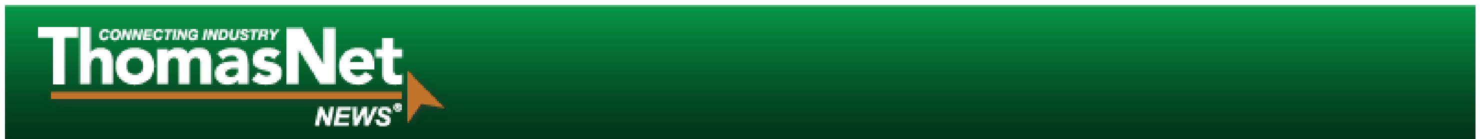

How Supply Chain Financing Is Changing Buyer-Supplier Relationships

by Jon Hansen | August 27th, 2014

Prominent business and supply chain analyst Jon Hansen says when buyers try to improve working capital position at the expense of suppliers, bad things happen usually. Supply chain financing is a tool that mutually benefits the positions of both stakeholders, creating win-win buyer-supplier situations.

Back in May I read a post by Eyal Rosenberg, CEO of payment automation software maker Nipendo, who made reference to an auto industry survey that highlighted the importance of supplier liquidity, including the negative impact that a slow payment process has on the buyer-supplier relationship. Specifically, Rosenberg pointed to the finding that automakersÂ *â€œthat maintain positive relationships with suppliers tend to offer the best products at affordable prices.â€*

This is an important correlation that for many years had been overlooked as a result of the disconnect between finance and purchasing.

Prior to procurement's recent elevation to beingÂ recognizedÂ forÂ its strategic importance to the overall enterprise, invoice payment was myopically managed within the confines of the finance department. Surely, purchasing would get involved with payment issues from time to time, when a key supplier refused to ship a needed item until outstanding invoices wereÂ paid. However, beyond situations of acute urgency, its involvement was minimal at best.

This is all changing now Â – and for the better.

The fact is that a healthy supply chain is, in reality, the life blood of the organization through which enterprise prosperity inevitable flows. If there is a breakdown in the supply chain, everything comes to a virtual stop. In short, a healthy supply chain means a healthy bottom line.

The question, of course, is how do you maintain a healthy supply chain that works at peak performance?

According to Jonas Schoefer, a director with working capital specialist firm REL, integrating supply chain financing into a business' operations creates a "positive effect on the overall health" of its supply chain.

Supply chain financing is a vehicle through which a third-party finance organization provides short-term credit that optimizes working capital for both the buyer and the seller. Usually involving the utilization of a purchase-to-pay (P2P) technological platform that automatically — and without human intervention — includes the management of the approval process as well as the settlement of invoices, supply chain financing has gained significant traction in recent years as a result of globalization. Industries at the forefront of supply chain financing adoption include automotive, manufacturing, and retail.

In referencing an REL survey, Schoefer indicated that the best companies have optimized their processes,Â enabling them to "pay suppliers two-and-a-half weeks later while also operating with nearly 70 percent less inventory." This means that even though companies using supply chain financing extend payables on the balance sheet, the suppliers are still able to access payments earlier, creating a "like-for-like trend in receivables" that extends throughout the entire end-to-end chain.

The result is obviously a more positive relationship between a buyer and its suppliers, leading to the benefits highlighted in the

automotive industry survey, including the “manufacturing of the best products at affordable prices.”

However, there are still challenges from the payer’s side of the equation in that only 14 percent of the companies that participated in the REL study indicated that they were able to improve days working capital for three consecutive years. For those unfamiliar with the term, days working capital reflects the number of days it takes a company to convert its working capital into revenue.

Said challenges notwithstanding, supply chain financing is a critical vehicle in terms of helping companies to improve their working capital positions without the risk of alienating suppliers.

The last point is particularly important given the case study from a CFO.com article by David M. Katz, titled “Six Ways To Extend Your Payment Terms.”

In the article, Katz writes about a large supermarket chain’s efforts to “stretch its payment terms” with a vendor from “21 days to 30 days.” The vendor responded by going to the press and insinuating that the retailer was experiencing cash flow problems. It was not exactly the response one would anticipate or appreciate.

Even though, in reality, the retailer’s financial position was stable, the vendor’s actions cast doubt on the financial health of the company.Â Ultimately, and with the involvement of senior management from both the retailer and the vendor, the matter was resolved.

However, there is an important lesson to be learned from this mouse-that-roared story. When an organization looks to improve its working capital position at the expense of its suppliers, the fallout can be far more costly than the anticipated gains.

Once again, this is where supply chain financing can and will play an important role that will enable all stakeholders to realize a mutually beneficial return on their relationships.

As the editor and lead writer for the PI Social Media Network’s Procurement Insights Blog, Jon Hansen has written close to 3,000 articles and papers as well as five books on subjects as diverse as supply chain practice, public sector policy, emerging business trends, and social media. A much sought-after speaker internationally, Jon is the host PI Window on The World Show on Blog Talk Radio, which will air its 900th episode in 2014. A two-time Ottawa Finalist for the Ernst & Young Entrepreneur of the Year Award, Jon was named by Blog Talk Radio as one of their top 300 hosts. He can be reached via http://procureinsights.wordpress.com and jhansen@pisocialmedia1.com.Â

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